ASSET MANAGEMENT

market notes: Onebridge... from Traditional to Digital

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coinbase ASSET MANAGEMENT

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1. Globalization is surging despite the fashionable arguments around deglobalization of traded goods. And the areas where globalization is strongest are critical to deepening digital technologies and supporting exponential growth in international connectivity. World exports of computers and communication services have nearly doubled as a share of GDP in the past twenty years. This has facilitated an explosion of cross-border data flows, up 10-fold in the past decade. Digital assets and the infrastructure around them will thrive in this global ecosystem.

2. We need platforms today for tomorrow's future, and we already have some. Protocols for micropayments and decentralized financial intermediation are past proof-of-concept stages. Let us contemplate growth in digital asset valuations to $8 trillion from the current $1.3 trillion over the next ten years, a 20% annualized growth pace. That growth pales in comparison to the opportunity from traditional assets migrating to digital forums. With over $400 trillion in global financial wealth, the sky is the limit.

3. It is the digitalization of traditional assets that will cement the place of newly formed infrastructure in the digital ecosystem. Why? Because it is a better user experience. Investors will have control over all assets with more flexibility of movement and return. Want to use a wider array of portfolio assets to collateralize borrowing? Or find liquidity for a fractional piece of a private asset? Digital will help. It is the utility of the technologies that will enhance user experience and catapult adoption. Conventional assets will awaken minds to the potential of digital. But the infrastructure to bridge traditional to digital had not existed. Until we built it.

4. Onebridge is built to capture financial services by linking the digital and traditional asset markets. Regulatory frameworks are a design feature, not a friction. Onebridge integrates contract law, the default and recovery process, securitization, and secondary trading capabilities natively into a blockchain workflow. The initial prototype focuses on discount notes broadly, and commercial paper, specifically because commercial paper is not a security. This allows Onebridge to focus on product-market fit with regulatory clarity and engagement.

5. How does Onebridge work? Figure 1 illustrates the flow of funds for a loan. A borrower creates a loan request with a reserve price. Investors can bid on the loan, submitting funds and limit prices on the Ethereum blockchain. An auction runs automatically by way of a smart contract, with funds transferred to the borrower alongside a non-transferable obligation token.

Settlement is virtually instantaneous and final. Investors receive rights tokens for their pro-rata share of the loan obligation, which are tradeable in a secondary market. At maturity, the loan is repaid, funds are distributed to rights token holders automatically, and tokens are extinguished. This is the simple life cycle of a loan in digital form, from beginning to end.

6. But what happens if the life cycle of the loan ends without a repayment, in default? This is where smart contract technologies shine. Missed repayments are programmed directly into the rights tokens. In the event of default, obligation tokens cannot be retired whereas rights tokens held by investors are freely tradeable to find liquidity pools that specialize in delinquency trading. A stressed and distressed asset market is created automatically. Capital migrates to investors who are built to manage distressed risks in short order, a potentially far more efficient process. Of course, the practical reality is that delinquency in the commercial paper market is rare. But even testing a one-day postponement of payment is a useful exercise.

7. The efficiency of on-chain finance is clear. Capital can be fluidly raised and retired through a network, on a moment's notice, at a fraction of the cost. But the transparency is also notable. Figure 2 illustrates the Etherscan – Ethereum's analytics platform for decentralized smart contracts – from a sample Onebridge transaction. The transaction hash captures all relevant information imprinted on the blockchain. The smart contract is what participants interact with. And the tokens created in the process of the transaction are all listed, including a digitalized token dollar ('tokenc'), the obligation token of the issuer, and the market value of the rights token held by two investors in this case.

8. Onebridge imports the open philosophy of the digital world into the traditional one. It is not the tokenization of commercial paper – it is turning paper into a natively digital asset. Of course, as was the case with bitcoin and other protocols, Onebridge starts with a walled garden approach. Participants in the network will be vetted as qualified institutional buyers, the initial secondary market will be limited by the same narrow starting point. Regulators will guide requirements for dynamic compliance solutions. It is infrastructure and it works. Over time the walls will come tumbling down for a more open, compliant network.
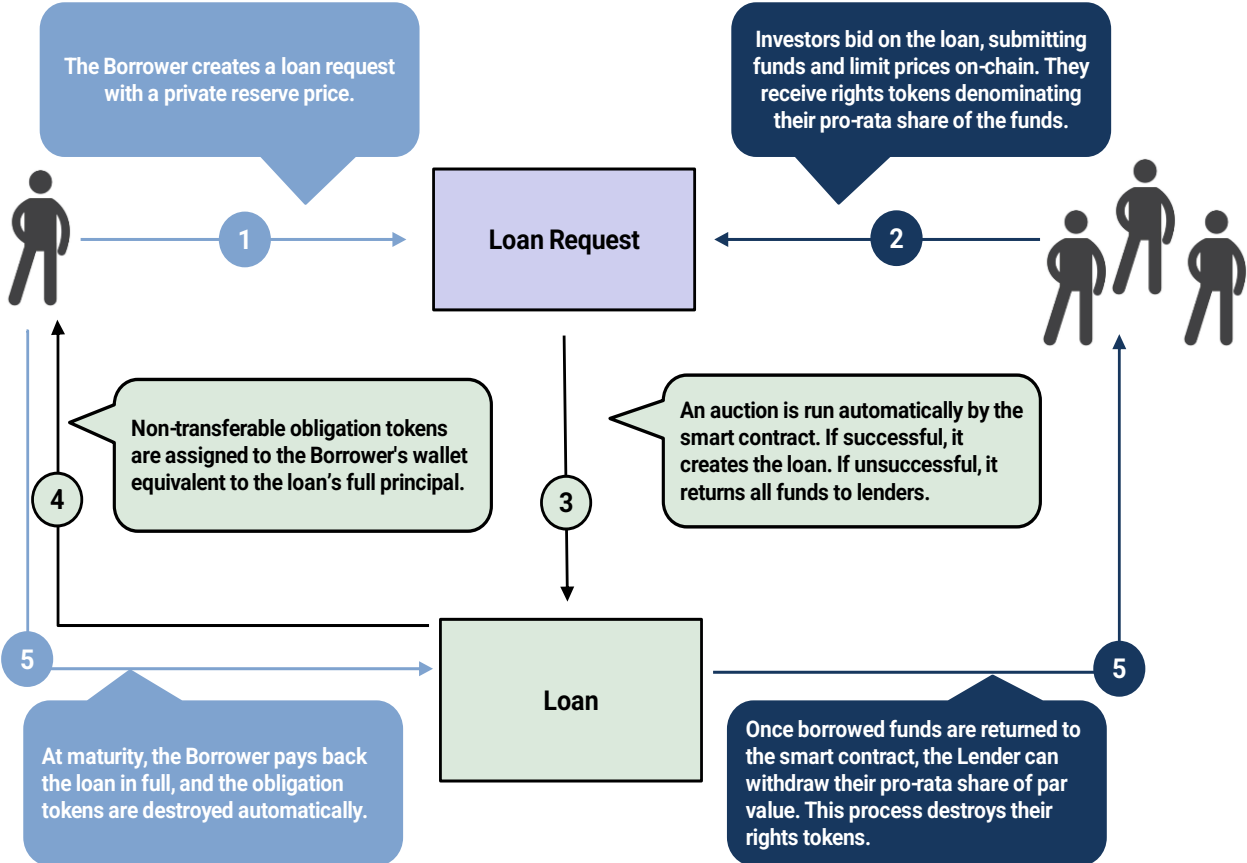
9. We are building upon the success of decentralized finance. Those protocols demonstrated mechanisms to share economics across a network and risk-manage exposures by way of mathematics to enhance financial stability. The protocols were not designed to serve as a bridge to traditional finance nor to regulatory entities. They were designed to add velocity, return, and risk to holdings of native digital assets. To enter the mainstream, features such as regulatory compliance are front-and-center, and the current network of users are unlikely to embrace such an approach.

10. Onebridge is a window into a radical improvement to financial intermediation, not a radical redesign of the monetary system. Digitalizing assets allows for more efficient coordination between the users and providers of capital and shared economics to those adding value to the network through engagement. Financial services are changing. Competition will focus on providing services for assets under the control of their owners in the future. Efficiency, control, and choice will be the hallmarks of a new era. We are inviting broad participation into that future

by starting Onebridge with a lower-risk, familiar asset. The Onebridge network will learn together and grow to handle more complexity over time. Join us.

Figure 1 – Onebridge Flow of Funds, Integration of Law, Issuance, Trading and Recovery

Source: One River Digital Asset Management.

Figure 2 – Etherscan Record from On-Chain Transaction

⑦ Transaction Hash:	0x3639b30f3b143f683b579cb92c6bd61328420698011dc617aa80d939697022bb 🗐
⑦ Status:	✅ Success
⑦ Block:	31354700 21 Block Confirmations
⑦ Timestamp:	🕐 1 min ago (May-01-2022 05:44:16 AM +UTC)
⑦ From:	0x1c899610741d17459d22e066222527702d075773 🗐
⑦ Interacted With (To):	🔍 Contract 0xe832622fcc981e3e2b292d9a0cfa16e69898c0fa ✅ 🗐
⑦ Tokens Transferred: ⑥	▸ From 0x1c899610741d1... To 0xe832622fcc981... For 1,100,000,000 ◑ tokenc (tokenc)
	▸ From 0x1c899610741d1... To 0x0000000000000... For 1,100,000,000 ◑ uObligationT... (uoToke...)
	▸ From 0x42850d027ed8d... To 0x0000000000000... For 497,625,000 ◑ rightsToken (rToken)
	▸ From 0xe832622fcc981... To 0x42850d027ed8d... For 500,000,000 ◑ tokenc (tokenc)
	▸ From 0x12a3297534d40... To 0x0000000000000... For 597,150,000 ◑ rightsToken (rToken)
	▸ From 0xe832622fcc981... To 0x12a3297534d40... For 600,000,000 ◑ tokenc (tokenc)

Source: One River Digital Asset Management.

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